Item 455-B-2

UNITED STATES DEPARTMENT OF EDUCATION
WASHINGTON, D.C. 20202

August 1989

89-S-59
89-L-132
89-G-167

SUMMARY: Questions and answers regarding the June 5, 1989 final regulations implementing the Secretary's Default Reduction Initiative.

Dear Colleague:

On June 5, 1989, the Secretary published final regulations in the Federal Register addressing the issue of defaults in the Stafford Loan and Supplemental Loans for Students (SLS) programs. The Secretary recently sent a letter to the president of each school in the program notifying the school of its Fiscal Year (FY) 1987 default rate and outlining the steps it must take to reduce defaults by its students in light of that default rate.

Enclosed with this letter is a set of questions and answers addressing a number of issues that have been raised by the public regarding the new regulations. We are also preparing a separate Dear Colleague letter addressing issues relating to the treatment of institutional refunds. That letter will include guidance on questions that have been raised regarding pro rata refund rules included in the new regulations.

We would like to call your attention to two items contained in the attached set of questions and answers. First, as noted in Q & A No. 2 in the Default Rate Calculation section, any school that has been converted from a component of another school into a separate school since October 1, 1987, is subject to the consequences, if any, of the FY 1987 default rate calculated for its former parent school. Such a new school should promptly contact its former parent school to find out whether the former parent school is subject to any such consequences.

Second, each guarantee agency must respond to the Secretary's request that it provide the Secretary with its recommendations on the appropriate default management plan for each school from which it receives default-related information required by the Secretary's recent letter to the school within 30 days of receipt of that information. An agency's failure to provide these recommendations on a timely basis may prevent these recommendations from being considered in the Secretary's development of a default management plan for the school.

If you have additional questions or concerns regarding the contents of this letter, please contact Pat Newcombe of this office.

Sincerely,

Roberta B. Dunn
Deputy Assistant Secretary
for Student Financial Assistance

William L. Moran
Director, Student Financial
Assistance Programs

Enclosure

Delayed Certification of Loan Applications (34 CFR 682.603(c))

1. Q. May a school that has a default rate of 30 percent or less choose to implement the delayed certification process required of schools with rates over 30 percent?

A. Any school may implement this procedure as long as the school does not refuse to certify an application for an otherwise eligible borrower.

2. Q. May a school that is subject to the delayed certification requirement deliver some loan proceeds to the student earlier than the regulations permit based on a student's special circumstances?

A. No.

3. Q. Does the delayed certification requirement require a school to delay certification of the loan application until the student has attended class for 30 days in the period of enrollment for which the loan is made?

A. No. The regulations only require that a school deliver loan proceeds to the borrower after the 30th day of the period of enrollment for which the loan was made. The school must only delay its certification of the loan long enough so that the delivery of the proceeds may take place more than 30 days into the enrollment period without violation of the "prompt delivery" rule set forth in 34 CFR 682.604(c). The borrower is not required to have attended class for each day in the 30-day period, as long as the borrower has maintained eligibility for the loan, as required by §682.604(b)(4).

Initial Counseling (34 CFR 682.604(f))

1. Q. May a school include in its initial loan counseling a written test of the student's understanding of the terms and conditions of the loan, and refuse to certify a loan application until the prospective borrower earns a passing score on the test?

A. A school may administer such a test, and may require a student that fails the test to undergo intensive additional counseling. However, a school may not refuse to certify a loan application based on the student's failure to pass that test.

2. Q. May a school supplement its required initial counseling with other counseling tools, such as interactive self-instructional computer programs?

A. A school may use other tools to supplement the required in-person or videotape initial counseling session.

3. Q. Does the regulatory requirement that "an individual with expertise in Title IV programs be reasonably available shortly after the counseling" require that an individual be available in person immediately after the counseling session?

A. Such an individual does not have to be available in person at that time, but an adequate number of such individuals must be easily accessible to students shortly after the session, either in person or by telephone, to answer questions.

4. Q. Must a school that is not a correspondence school provide the required in-person or videotape initial counseling to students attending classes at remote locations a significant distance from the school's financial aid office? May a school use the counseling procedures applicable to correspondence schools with respect to a student enrolled in an "external degree" program that does not require the student's presence on a campus of the school, or with respect to a student participating in a junior year abroad or similar exchange program?

A. A school that is not a correspondence school must provide the required in-person or videotape initial counseling to students at remote locations. However, a school may follow the counseling procedures for correspondence schools with respect to students in "external degree" programs, junior year abroad programs, and similar off-campus programs.

5. Q. May a lender or guarantee agency representative conduct required counseling on behalf of the school or otherwise assist school personnel in conducting required counseling? If so, must that representative be compensated?

A. A lender or guarantee agency representative may conduct or assist in conducting required counseling sessions, on behalf of the school, but that representative must be reasonably compensated by the school to avoid a violation of the anti-inducement provisions of the Higher Education Act of 1965, as amended (the Act) See sections 428(b)(3) and 435(d)(5) of the Act. If the representative merely supplements the school's required counseling, the representative would not have to be compensated.

6. Q. The instructions for calculating a school's placement rate under §668.44(c)(1)(iii) state that a school must use "...students who were originally scheduled at the time of enrollment to complete the program...." However, that provision also states that the school should treat "any graduates" for whom they do not have documented evidence of employment as not having obtained employment. Why do the regulations address both "students" and "graduates?"

A. The reference to "graduates" in that paragraph, in §§668.15(b)(2)(ii)(A) and 668.44(c)(1)(ii), and in the Track Record Disclosure Forms, should have been to "students." The Secretary is promulgating a technical correction to the regulations and Track Record Disclosure Forms to correct this error.

7. Q. May a school comply with the initial counseling requirements merely by having an employee provide its first-time borrowers with printed counseling materials?

A. No. Although such information may be used to supplement a counseling session, the mere presentation of printed material to students by a school representative does not satisfy this requirement.

Track Record Disclosures (34 CFR 668.44(c)-(f))

1. Q. If a State licensing agency will not release information to a school that the school needs to calculate the pass rate of its students on the State licensing examination, what should that school do to comply with §668.44(c)(ii), which requires that the institution disclose that rate to prospective students?

A. A State licensing agency's written refusal to provide this information excuses the school from compliance with §668.44(c)(ii) for the year or years for which the agency refuses to provide the information. The school should note on an attachment to the Track Record Disclosure Form that the State licensing agency has refused to provide this information.

2. Q. In calculating the State licensing examination pass rate, should the school use the rate for those of its students who both graduated and sat for the examination during the calendar year in question, or should the school use the rate for all of its graduates who sat for the examination during that period, including those who completed the program in a previous calendar year?

A. The pass rate required to be disclosed is the pass rate for all graduates who took the exam in a given year, regardless of the year in which they completed the program.

3. Q. In calculating completion rates, how should a school treat a part-time student or a student who receives a leave of absence?

A. The "amount of time normally required to complete the program" is calculated on a pro rata basis for periods of less than full-time enrollment status, but is not increased by any period during which the student receives a leave of absence.

4. Q. Must a school provide the required disclosures to all prospective students enrolled in programs subject to §668.44 (c) - (d) or are those provisions applicable only to Title IV recipients?

A. The school must provide all prospective students enrolled in an eligible program with the required disclosures. NOTE: The Secretary is promulgating a technical correction to the effective dates for certain portions of the disclosures. The disclosures to be made under §668.44(c)(1)(ii)-(iv), including disclosures to which those paragraphs apply by operation of §668.44(d)(1), apply only to students in eligible programs covered by the regulation with respect to periods of enrollment beginning on or after December 1, 1989.

5. Q. What disclosures must a school make for a new program under 668.44(c)-(d)?

A. If a program has not been in existence long enough for a statistic to be calculated under §668.44(c) or (d), that statistic need not be disclosed until such time as it can be calculated under the regulations. The school should enter "N/A" in the space for that statistic on the Track Record Disclosure Form and explain in an attachment to the Form that the program is too new for that information to be available.

6. Q. Are the new consumer disclosure requirements in §668.44 applicable only to vocational schools?

A. These requirements apply to all types of schools with respect to all eligible undergraduate non-baccalaureate degree programs designed to prepare students for a particular vocational, trade, or career field.

7. Q. Do the disclosures of completion rates, job placement rates, and State licensing examination pass rates apply to a school offering an Associate degree program? What if that program is offered both as a terminal degree program and as a transfer program fully acceptable for credit toward a baccalaureate degree under an agreement with a four-year institution?

A. The required disclosures apply to any program for which a school publicly makes a claim as to the job placement experience of its students. The disclosures also apply to any undergraduate nonbaccalaureate degree program designed to prepare students for a particular vocational, trade, or career field.

The principal goal of these requirements is informed consumer choice. In keeping with this objective, the Secretary intends these requirements to apply to any program that is marketed, promoted, or otherwise represented to the public (e.g. in school publications) as a program the completion of which prepares the student for employment in a particular vocational, trade, or career field. This representation may be explicit, or may be implicit in the nature of the program (e.g. a program offering a certificate in Auto Mechanics). If this representation is present, the disclosures must be provided, regardless of whether the credits earned in the program are partially or fully transferable toward a baccalaureate degree at that school or elsewhere. However, in an attachment to the Track Record Disclosure Form, the school may indicate the number of students in the program who are treated as nonplacements for purposes of the placement rate calculation who have completed the program and transferred to a baccalaureate degree program.

8. Q. May a school modify or add additional information to the Track Record Disclosure Form that must be used to make the consumer disclosures ? Is a separate form required for each program for which these disclosures must be made.?

A. A school must use the applicable form as it appears in the Appendix to this bulletin. The contents cannot be modified in any way, except to replace appropriate parenthetical material with the appropriate information. A separate form must be used for each program for which the school must make these disclosures.

9. Q. How is the term "students" defined for purposes of calculating the job placement and completion rates under 668.44(c)(1)(iii) and (iv)? Are "no shows" included?

A. For the purpose of calculating these rates, the term "students" includes all enrollees that in fact commence attendance (i.e. attend class, submit a lesson or paper, or take an exam) in the program for which the disclosures are made. A "no show" need not be included as a "student" in these calculations.

10. Q. May a school disclose a completion rate, job placement rate, or State licensing examination pass rate for a more recent calendar year than the year described in §668.44(c)?

A. Yes, as long as the same year is used for the job placement rate and completion rate disclosed to the student.

11. Q. Where should a school send the track record and cost information required to be submitted to the Secretary under 34 CFR 682.610(g)?

A. This information must be sent to Mr. Brian Kerrigan, U.S. Department of Education, ROB-3, Room 4624, 400 Maryland Avenue, S.W., Washington, D.C. 20202-5132.

Default Rate Calculations and Consequences of Default Rates (34 CFR 668.15)

1. Q. Is the fiscal year default rate calculated for a school a combined rate that includes both the Stafford Loan and SLS programs? Is a student who receives both a Stafford loan and an SLS loan and defaults on both loans counted as one or two defaults in the school's fiscal year rate? How will students who borrow for attendance at more than one school be reflected in the schools' default rates?

A. The default rate for a school calculated under the regulations is a combined rate for both the Stafford Loan and SLS programs. A student who defaults on more than one loan during the period covered by a single fiscal year default rate calculation is counted as one default in the school's default rate for that fiscal year. If a student borrowed for attendance at more than one school, the student's repayment or subsequent default is attributed to each school for attendance at which the student received a loan that entered repayment in the fiscal year for which the rate is calculated.

2. Q. How will rates be calculated for schools with several locations? How will default rates be calculated for, and the consequences of high default rates apply to, schools or locations that have recently undergone a change of ownership, a conversion from a "branch campus" to a freestanding school or vice versa, or a conversion from a branch of one school to a branch of another?

A. Under the regulations, a default rate is calculated for each holder of a Program Participation Agreement. However, the Department's computer system is designed to calculate a rate for each holder of a GSL program school identification number. In the vast majority of cases, these two approaches are identical. However, a few schools retain separate identification numbers for their various components (i.e. locations or divisions) while operating under a single school-wide Program Participation Agreement. For these schools, the Secretary has recently calculated and notified each component with its own identification number of its default rate. Such a school may calculate its school-wide rate by computing the weighted average of the rates for the various components for which individual rates were supplied. The weighted average is calculated by multiplying each component's rate by the number of borrowers on which it is based, calculating the sum of those products, and dividing by the total number of borrowers on which the rates were based.

The school may choose to use the weighted average rate as the school's actual rate for purposes of the regulations. The use of that rate may result in different treatment for the school or component of the school than the treatment described in the Secretary's default rate notification letters to the school's components. To use the weighted average rate, the school must notify the Secretary that it wishes to do so. Upon receipt of that notification, the Secretary will provide a revised notice to the school of the treatment of the school that results from the weighted average rate. Schools wishing to use this option must send notification to that effect to Mr. Brian Kerrigan, U.S. Department of Education, ROB-3, Room 4624, 400 Maryland Avenue, S.W., Washington, D.C. 20202-5132.

The default (or lack thereof) by a student that borrows for attendance at a school or a component of a school is charged (or credited) to the school whose identification number appears on the loan application. This holds true even if the loan enters repayment after the school or component has been sold, the component has been converted into a separate school, or the school or component has been converted into a component of another school.

The consequences of a default rate for a school -- whether it involves a default management plan, required refund and loan certification procedures, or exposure to administrative sanctions -- apply to all components (i.e. divisions and locations) of the school from the date the school is notified of that rate until the date that the consequences no longer apply to the school. The consequences of a school's rate also generally apply to all components of the school as it exists on the first day of the fiscal year for which the rate is calculated. This latter principal holds true even for (1) a component that, prior to the imposition of the default management plan, refund and

certification requirements, or administrative sanctions, is converted to a separate school, and (2) a school that, prior to such imposition, is converted to a component of another school. However, if a component of a school is converted to a component of another school, whether or not a change of ownership is involved, the consequences of the first school's default rate do not apply to the component after that conversion.

If an entire school undergoes a change of ownership that results in a change in control, the consequences of its default rate for the fiscal year in which the change of ownership occurs, and prior years, apply to the school after the change only if the change results in its being considered to be the same institution under 34 CFR 600.31. If the new school is not considered to be the same institution, the consequences of the old school's rate do not apply to the new school.

> Example 1: School A's Fiscal Year (FY) 1987 default rate -- that is, the percentage of the school's borrowers entering repayment in FY 1987 that defaulted before the end of FY 1988 -- is over 30%. All components of the school as it existed on October 1, 1986 are therefore required to implement the pro rata refund and delayed certification requirements pursuant to the Secretary's recent notice to the school. A component of School A that became a separate school on or after October 1, 1987, is subject to those requirements for as long as they apply to School A.

NOTE: As the above example shows, any school that has been converted from a component of another school to a separate school since September 30, 1987, should promptly contact the school of which it was formerly a part to find out whether the new school is subject to any consequences of the FY 1987 default rate calculated for its former parent school.

> Example 2: School B changes ownership and control. If the new owners satisfy the requirements of 34 CFR 600.31(a), the school is considered to be the same school notwithstanding the change in ownership. In that event, the school's identification number does not change, and it is subject to the consequences of the default rate calculated for the school for the fiscal year in which the change of ownership occurred, and any other fiscal year. If the new owners do not satisfy the requirements for the school to be considered the same school, then the post-ownership change school is considered a new school, receives a new identification number when it is admitted into the program, and is not subject to the consequences of any default rates calculated for the pre-ownership change school.

> Example 3: School A sold one of its locations to School B on January 1, 1988. Since School A's FY 1987 default rate is over 30%, it is notified in August 1989 that it must implement pro rata refunds and delayed loan certification. Those requirements do not apply to the location sold on January 1, 1988, since it has been converted to a component of another school. However, that component is subject to any consequences of School B's FY 1987 default rate since it is now a part of School B.

The Secretary reserves the right to disregard the corporate form of a school or the manipulation thereof, as permitted by applicable law, in cases where to do so would prevent circumvention of the regulations or otherwise serve the public interest.

3. Q. What steps should a school take if it believes its fiscal year default rate as calculated by the Secretary is inaccurate? Will the Secretary provide the school with the data on which that calculation is based?

A. Instructions for contesting the determination that a school's rate exceeds 30 percent are provided in the "Dear President" letter recently sent to each school in August 1989, which also included the Secretary's notification to the school of its FY 1987 default rate. A school wishing to contest the determination that its FY 1987 default rate exceeds 20 percent may do so as a part of the informal hearing available prior to the Secretary's imposition of a default management plan. Upon written request, the Department will provide a school with the data used to calculate its default rate free of charge, if the school's FY 1987 rate exceeds 20% and the school had more than 30 borrowers who entered repayment during that fiscal year.

4. Q. Does the Department plan to produce a comprehensive national listing of FY 1987 default rates for use by guarantee agencies ?

A. A national listing of default rates for participating schools was sent to guarantee agencies at the same time that individual schools were notified of their rates.

5. Q. Is a school that is required by regulation to implement a pro rata refund policy and delayed certification of loan applications based on the fact that its FY 1987 default rate exceeded 30 percent released from those requirements once it is notified that its rate for a subsequent fiscal year is less than 30 percent.

A. A school would be released from those requirements as of the date of notification by the Secretary that its rate has dropped to 30 percent or less. However, if those requirements also appear in the default management plan imposed on the school by the Secretary, the school must continue to use those default reduction measures until the expiration of its plan.

6. Q. What is the role of the guarantee agencies in the development of default management plans for high default schools?

A. The Department recently notified schools with FY 1987 default rates between 20% and 40% that they must provide certain information to the Secretary and guarantee agencies to assist the Secretary in deciding on the contents of the plan for each school. Guarantee agencies are hereby requested to provide the Secretary with their recommendations for each school from which they receive this information within 30 days of receipt of the information. The agency's recommendations should include suggestions as to the content of the school's plan, if any, and a justification for any deviations in the suggested plan from Appendix D to 34 CFR Part 668, and should be sent to

Mr. Brian Kerrigan, U.S. Department of Education, ROB-3 Room 4624, 400 Maryland Avenue, S.W., Washington, D.C. 20202-5132.

7. Q. In the Secretary's recent letters notifying schools of their fiscal year 1987 cohort default rates, each school with a rate greater than 20 percent but less than 30 percent was provided with two options for developing a default management plan. Option 1 allows the school to develop its own default management plan. As part of the process of developing its plan under Option 1, a school was asked to justify any deviations from Appendix D in its proposed plan, as well as to provide the default analysis under §668.15(b)(2)(i) and the statistical analysis under §668.15(b)(2)(ii). A school that chooses to adopt all of the measures listed in Sections I and II of Appendix D does not have to provide these analyses, but still must justify its deviations from the remainder of Appendix D. Option 2 permits a school simply to adopt Appendix D as its plan.

May a school with less than a 30 percent default rate adopt Appendix D as its default management plan under Option 2 without implementing the delayed certification and pro rata refund default reduction measures in Section I, since those requirements automatically apply by regulation only to schools with default rates greater than 30 percent? If not, what information must a school provide to justify not adopting these two measures? In addition, for a default management plan developed under Option 1, must a school that does not offer undergraduate non-baccalaureate degree programs designed to prepare students for a particular vocational, trade, or career field provide both the default analysis and the statistical analysis described in the notification letter?

A. A school with a default rate of less than 30 percent that elects to adopt Appendix D as its default management plan under Option 2 must implement all the requirements listed in Appendix D, including delayed certification and pro rata refunds. If a school decides to develop a default management plan under Option 1 that includes all the requirements in Section I and II of Appendix D, it must also implement pro rata refunds and delayed certification as part of its plan as these two items are integral parts of Sec+

If a school developing a default management plan under Option 1 does not wish to implement delayed certification, pro rata refunds, or other measures in Appendix D, it must provide a detailed justification in its submission to the Secretary for all of the deviations from Appendix D in its plan. This must be done by showing either that the causes of default addressed by the measures proposed for exclusion do not cause a significant portion of defaults at the school, or that the excluded measures would not substantially reduce the defaults attributable to these causes. The measures in Section I of Appendix D are all steps designed to reduce defaults by dropouts. Thus, a school with a default rate of less than 30 percent may be subject to the pro rata refund and delayed certification provisions unless the school shows that defaults related to dropouts are not a significant cause of default at the school, or that those measures will not substantially reduce defaults by the school's dropouts.

Under Option 1, a school with a default rate of less than 30 percent that wishes to adopt a default management plan that does not include pro rata refunds, delayed certification, or another measure listed in Section I or II of Appendix D, must also provide the Secretary with the default analysis described in §668.15(b)(2)(i). In addition, if it offers undergraduate non-baccalaureate programs designed to prepare students for a particular vocational, trade, or career field, the school must provide the statistical analysis described in §668.15(b)(2)(ii). If a school with a rate of less than 30 percent wants to exclude pro rata refunds or delayed certification from its plan, and the school is not required to submit the statistical analysis under §668.15(b)2)(ii), the school's default analysis should include information and supporting data on the completion rate of the school's students for the three most recent calendar years ending not less than six months prior to the Secretary's request for this information. If that rate is calculated differently from the method set forth in §668.44(c)(1)(iv), the school should explain fully how it calculated that rate, particularly with regard to its treatment of lengthy leaves of absence and extended absences by students that never officially withdraw. The Secretary will use this information in determining whether to approve the school's proposed plan or whether that plan should include the provisions in question.

8. Q. In the Secretary's recent letters to schools with default rates between 40 percent and 60 percent, each school was notified that, if its fiscal year 1990 default rate falls in this range, it may be subject to administrative action by the Secretary to limit, suspend, or terminate (LST) its eligibility to participate in the Title IV programs. A similar notice was included in the letters to schools with rates above 60 percent, with regard to LST sanctions based on fiscal year 1989 rates. Do these notices apply to schools that have less than 30 borrowers entering repayment?

A. Yes. All provisions of the regulations apply to all schools, even those with less than 30 borrowers entering repayment per year. However, in order to avoid the unfairness and fluctuations in single year default rates that can occur with a school with a small number of borrowers, under §668.15(f)(1), if a school has less than 30 borrowers entering repayment in a fiscal year, its rate for that fiscal year will be calculated as a three-year average rate. This three-year average rate is the rate that is used for LST purposes, as well as for purposes of determining the applicability to the school of default management plan, pro rata refund, and delayed certification requirements based on that year's rate.

For example, a school with less than 30 borrowers entering repayment in fiscal year 1989 will have its fiscal year 1989 default rate calculated as the average of its single year rates for fiscal years 1987, 1988, and 1989. If that three-year average rate for fiscal year 1989 exceeds 60 percent, the school will be subject to LST action in 1991 on that basis. If that rate is between 40 percent and 60 percent, the school's fiscal year 1990 rate must be at least five percentage points lower to avoid LST action in 1992. If the school has less than 30 borrowers entering repayment in fiscal year 1990, then its fiscal year 1990 default rate will also be calculated as a three-year average rate, based on the single year rates for fiscal years 1988, 1989, and 1990.

9. Q. If a school is required to submit the comprehensive analysis of its causes of default and the statistical analysis to support its default management plan, what must it do to gather the information necessary for those analyses?

A. A school is not required to contact individual borrowers to determine why they did or did not default for purposes of the required analysis of causes of default, nor is it required to survey former students to determine the placement rate or State exam pass rate for prior years for purposes of the statistical analysis. However, the school should be able to obtain State exam pass rate information from the State, and should have the other required information in its records.

Appendix

Form I:

HOW OUR STUDENTS ARE DOING

To help you make a good decision about whether to sign up for (name of program), (name of institution) wants you to know that, according to the latest information--

---

_____%, or ___ of the _____ students in this program scheduled to graduate in (year) went on to graduate;

*_____%, or __ of the ____ students scheduled to graduate in that year have found jobs in (name of occupation or field for which training is offered); and

_____%, or __ of the _____ students in this program taking the (name of test) administered by the State of (name of State in which the program is being offered to the student) in (year) passed that examination.

Form II:

HOW OUR STUDENTS ARE DOING

To help you make a good decision about whether to sign up for (name of program), (name of institution) wants you to know that, according to the latest information--

---

_____%, or ___ of the _____ students in this program scheduled to graduate in (year) went on to graduate; and

*_____%, or __ of the ____ students scheduled to graduate in that year have found jobs in (name of occupation or field for which training is offered).

I have read and understood the graduation rate and job information provided above.

_____ (Prospective student's signature)

Date

* We have been told by ____ of the students scheduled to graduate in that year that, even though they graduated, they decided not to look for a job in that occupation. Also, ____of the students scheduled to graduate in that year have not responded to our job placement questionnaire, so we do not know whether they have found jobs or not.